

Legislative Audit Division

State of Montana



Report to the Legislature

November 2006

Financial Audit

For the Fiscal Year Ended June 30, 2006

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Montana Guaranteed Student Loan Program

Office of the Commissioner of Higher Education

We performed a financial audit of the Montana Guaranteed Student Loan Program's Federal Special Revenue Fund for the fiscal year ended June 30, 2006. This report contains the audited financial statements and accompanying notes for fiscal year 2005-06. We issued an unqualified opinion on the financial statements. The opinion means the reader may rely on the financial statement information presented.

This is an annual financial audit performed to attest to the fairness of the financial statements the Montana Guaranteed Student Loan Program. Audit recommendations, if any, identified during this financial audit will be included in the biennial financial-compliance audit of the Office of the Commissioner of Higher Education (07-20).

Direct comments/inquiries to:
Legislative Audit Division
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06-06

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FINANCIAL AUDITS

Financial audits are conducted by the Legislative Audit Division to determine if the financial statements included in this report are presented fairly and the agency has complied with laws and regulations having a direct and material effect on the financial statements. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States Government Accountability Office. Financial audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) certificates.

Government Auditing Standards, the Single Audit Act Amendments of 1996 and OMB Circular A-133 require the auditor to issue certain financial, internal control, and compliance reports. This individual agency audit report is not intended to comply with these requirements and is therefore not intended for distribution to federal grantor agencies. The Legislative Audit Division issues a statewide biennial Single Audit Report which complies with the above reporting requirements. The Single Audit Report for the two fiscal years ended June 30, 2007, will be issued by March 31, 2008. The Single Audit Report for the two fiscal years ended June 30, 2005, was issued on March 6, 2006. Copies of the Single Audit Report can be obtained by contacting:

Single Audit Coordinator
Office of Budget and Program Planning
State Capitol
Helena MT 59620
Phone (406) 444-3616

Legislative Audit Division
Room 160, State Capitol
PO Box 201705
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Scott A. Seacat, Legislative Auditor
Tori Hunthausen,
Chief Deputy Legislative Auditor



Deputy Legislative Auditors:
James Gillett
Jim Pellegrini

November 2006

The Legislative Audit Committee
of the Montana State Legislature:

This is our report on the fiscal year 2005-06 financial audit of the Commissioner of Higher Education's Montana Guaranteed Student Loan Program (MGSLP) Federal Special Revenue Fund. The objectives of a financial audit include determining if the program's financial statements present fairly its financial position at June 30, 2006, and the results of its operations for the fiscal year. We tested compliance with state and federal laws that have a direct and material impact on the financial statements. Additional compliance testing for the program is included in our biennial financial-compliance audit of the Office of the Commissioner of Higher Education.

The MGSLP was authorized by the Montana legislature in 1979 and established July 1, 1980. The MGSLP allows eligible students to receive loans from lending institutions to pay for post-secondary education. The federal government guarantees the loans made by lending institutions and makes administrative cost reimbursements to the MGSLP for acting as a collection agent. The MGSLP performs the administrative duties associated with the loan guarantee process but contracts with an outside vendor for computer support services.

As of June 30, 2006, the original principal balance of guaranteed loans outstanding was approximately \$1,639,865,033, with a default rate of 0.98 percent for federal fiscal year 2005-06. Given the current default rate, the federal government will reimburse MGSLP 98 to 100 percent for loans issued prior to October 1, 1998, and 95 percent for loans issued on or after October 1, 1998.


Beginning on page A-1, you will find the Independent Auditor's Report followed by the financial statements and accompanying notes. We issued an unqualified opinion, which means the reader can rely on the presented information. The MGSLP's response to our audit is on page B-1.

We thank the Office of the Commissioner of Higher Education, the Director of the MGSLP, and their staff for the cooperation and assistance they provided during the audit.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Scott A. Seacat", with a long horizontal flourish extending to the right.

Scott A. Seacat
Legislative Auditor



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Director of Accounting and Budgeting

Montana Guaranteed Student Loan Program

Bruce Marks

Director

Karen Wing

Deputy Director/CFO

For additional information concerning the Montana Guaranteed Student
Loan Program, contact Bruce Marks, Director, at:

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Members of the audit staff involved in this audit were Pearl Allen,
Jeane Carstensen-Garrett, Alexa O'Dell, and Jeff Tamblyn.

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
Tori Hunthausen,
Chief Deputy Legislative Auditor



Deputy Legislative Auditors:
James Gillett
Jim Pellegrini

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying Balance Sheet of the Commissioner of Higher Education's Montana Guaranteed Student Loan Program – Federal Special Revenue Fund as of June 30, 2006, and the related Statement of Revenues, Expenditures, and Changes in Fund Balance for the fiscal year then ended. The information contained in these financial statements is the responsibility of the program's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Commissioner of Higher Education's Montana Guaranteed Student Loan Program – Federal Special Revenue Fund as of June 30, 2006, and the results of its operations for the fiscal year then ended, in conformity with accounting principles generally accepted in the United States of America.

Respectfully submitted,

A handwritten signature in cursive script, appearing to read "James Gillett".

James Gillett, CPA
Deputy Legislative Auditor

October 12, 2006

Montana Guaranteed Student Loan Program Financial Statements and Notes

**Commissioner of Higher Education
Montana Guaranteed Student Loan Program
Federal Special Revenue Fund
Balance Sheet
As of June 30, 2006**

	Agency Operating Fund	Federal Student Loan Reserve Fund	Essay Scholarship Fund
Assets			
Cash in Treasury	\$ 717,085	\$ 707,201	\$ 37,134
Short Term Investments (Note 2)	6,079,287	2,670,228	128,523
Accounts Receivable	253,889	48,092	2,108
Due From Federal Government (Note	50,336	3,168,552	-
Long Term Investments (Note 4)	-	-	26,341
Prepaid Expense	9,446	-	-
	<hr/>	<hr/>	<hr/>
Total Assets	<u>\$ 7,110,043</u>	<u>\$ 6,594,073</u>	<u>\$ 194,106</u>
 Liabilities and Fund Balance			
Liabilities			
Accounts Payable	\$ 847,678	\$ 105,326	\$ 2,108
Deferred Revenue	1,268	-	-
Property Held in Trust (Note 5)	183,577	-	-
Due to Federal Government (Note 6)	-	708,883	-
	<hr/>	<hr/>	<hr/>
Total Liabilities	<u>\$ 1,032,523</u>	<u>\$ 814,209</u>	<u>\$ 2,108</u>
 Total Fund Balance	 <u>6,077,520</u>	 <u>5,779,864</u>	 <u>191,998</u>
 Total Liabilities and Fund Balance	 <u>\$ 7,110,043</u>	 <u>\$ 6,594,073</u>	 <u>\$ 194,106</u>

The accompanying notes are an integral part of this financial statement.

Commissioner of Higher Education
Montana Guaranteed Student Loan Program
Federal Special Revenue Fund
Statement of Revenues, Expenditures, and Changes in Fund Balance
Budget and Actual
For the Period July 1, 2005 - June 30, 2006

	Agency Operating Fund			Federal Student Loan Reserve Fund			Essay Scholarship Fund		
	Budget	Actual	Variance	Budget	Actual	Variance	Budget	Actual	Variance
Revenue									
Guarantee Fee Income (Note 8)	\$ 706,321	\$ 657,639	\$ (48,682)	\$ 1,653,795	\$ 1,624,506	\$ (29,289)	\$ -	\$ -	\$ -
Loan Processing and Issuance Fee (Note 9)	1,316,118	1,829,196	513,078	-	-	-	-	-	-
Account Maintenance Fees (Note 10)	641,071	1,006,662	365,591	-	-	-	-	-	-
Default Aversion Fees (Note 11)	3,635,224	3,392,027	(243,197)	-	-	-	-	-	-
Collection Recoveries (Note 12)	2,713,473	2,699,117	(14,356)	-	-	-	-	-	-
Loan Rehabilitations (Note 12)	36,858	-	(36,858)	-	-	-	-	-	-
FFELP Consolidation Collections (Note 12)	1,304,102	1,088,279	(215,823)	-	-	-	-	-	-
FDSLP Consolidation Collection Fees (Note 12)	-	-	-	22,530,214	17,003,774	(5,526,440)	-	-	-
Reinsurance from Department of Education (NO	-	-	-	162,871	169,804	6,933	-	-	-
Non-Reinsured Loan Recoveries (Note 16)	190,675	167,796	(22,879)	-	-	-	-	-	-
Disbursement Service Fees (Note 5)	93,978	220,941	126,963	131,150	217,258	86,108	-	6,500	6,500
Investment Earnings (Note 2 & 4)	9,042	19,360	10,318	-	1,987	1,987	-	-	-
Miscellaneous									
Total Revenue	<u>10,646,862</u>	<u>11,081,017</u>	<u>434,155</u>	<u>24,478,030</u>	<u>19,017,329</u>	<u>(5,460,701)</u>	<u>0</u>	<u>6,500</u>	<u>6,500</u>
Expenditures									
Administrative Costs	\$ 5,914,400	\$ 4,837,886	\$ 1,076,514	\$ -	\$ 3,271	\$ (3,271)	\$ -	\$ 91	\$ (91)
Cost of Loan Collections (Note 12)	4,488,662	4,462,632	26,030	-	-	-	-	-	-
Claims Paid to Lenders (Note 13)	-	-	-	23,347,372	17,504,608	5,842,764	-	-	-
Default Aversion Fees (Note 11)	-	-	-	641,071	1,006,662	(365,591)	-	-	-
Account Maintenance Fee Expense (Note 10)	-	-	-	413,230	1,343,136	(929,906)	-	-	-
Scholarships	-	-	-	-	-	-	-	27,526	(27,526)
Total Expenditures	<u>10,403,062</u>	<u>9,300,518</u>	<u>1,102,544</u>	<u>24,401,673</u>	<u>19,857,677</u>	<u>4,543,996</u>	<u>0</u>	<u>27,617</u>	<u>(27,617)</u>
Excess (Deficiency) of Revenues Over Expenditures	243,800	1,780,499	1,536,699	76,357	(840,348)	(916,705)	-	(21,117)	(21,117)
Fund Balance 06/30/05	4,333,621	4,333,621	-	6,620,212	6,620,212	-	-	176,515	176,515
Transfer of Essay Scholarship Funds (Note 14)	(40,000)	(36,600)	3,400	-	-	-	0	36,600	36,600
Fund Balance 06/30/06	<u>\$ 4,537,421</u>	<u>\$ 6,077,520</u>	<u>\$ 1,540,099</u>	<u>\$ 6,696,569</u>	<u>\$ 5,779,864</u>	<u>\$ (916,705)</u>	<u>\$ 0</u>	<u>\$ 191,998</u>	<u>\$ 191,998</u>

The accompanying notes are an integral part of this financial statement.

**Commissioner of Higher Education
Montana Guaranteed Student Loan Program
Federal Special Revenue Fund
Notes to the Financial Statements
For the Fiscal Year Ended June 30, 2006**

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Description of Program

The State of Montana's Guaranteed Student Loan Program (MGSLP) is located in the Office of the Commissioner of Higher Education. MGSLP was established by the Office of the Commissioner of Higher Education in fiscal year 1981 to coordinate and administer the federally insured student loans issued by various lending institutions. Montana's Federal Family Education Loan Program (FFELP) operates in compliance with and pursuant to agreements between the Montana Board of Regents and the U.S. Department of Education (DE), pursuant to Section 428 of the Higher Education Act of 1965, as amended.

B. Basis of Accounting

The financial statements were prepared using the modified accrual basis of accounting, and are presented in a budget to actual format, which does not significantly differ from a GAAP presentation. Under the modified accrual basis of accounting, expenditures are recorded on the basis of valid obligations. Revenues are recorded when received in cash unless susceptible to accrual. Revenues are susceptible to accrual if they are measurable and available to finance expenditures of the fiscal period or are not received at the normal time of receipt. The budget information presented in the Statement of Revenues, Expenditures, and Changes in Fund Balance – Budget and Actual is as approved by the Montana Board of Regents for fiscal year 2006.

C. Descriptions of Federal Special Revenue Funds

As a Federal Special Revenue Fund, MGSLP accounts for the proceeds of revenue sources that are legally restricted to expenditures for specified purposes. Pursuant to the Higher Education Act of 1965, as amended, MGSLP accounts for its operations in two separate funds: the Federal Student Loan Reserve Fund (FSLRF) and the Agency Operating Fund (AOF). Use of the FSLRF is limited to payment of lender claims and payment of default aversion fees or other DE fee payments as directed. MGSLP is required to deposit claim reimbursements from DE into the FSLRF, as well as the following: DE's equitable share of defaulted loan recoveries, the portion of default recoveries that equals the complement of the reinsurance rate which is not reimbursed to MGSLP by DE, and student loan insurance premiums (guarantee fees). The AOF is the property of MGSLP and is used for a variety of FFELP activities and for other student aid related activities as selected by the agency. Payments received by MGSLP for loan processing and issuance, account maintenance, default aversion activities, and MGSLP's share of defaulted loan collections is all deposited into the AOF. MGSLP also maintains a fund to account for funds held in trust for recipients of MGSLP's essay scholarship contest. Funds are invested in certificates of deposit of varying maturity dates with the Montana Family Education Savings Program or in the Montana Short Term Investment Pool (STIP).

2. SHORT TERM INVESTMENTS

Short Term Investments are units purchased in the State of Montana's Short Term Investment Pool (STIP) and are reflected at cost, which equals market. The Board of Investment's policy requires that STIP securities have the highest investment grade rating in the short-term category by at least one Nationally Recognized Statistical Rating

Organizations. STIP has a portfolio rating of A1+. The STIP Investment Policy Statement does not specifically address concentration of credit risk. As of June 30, 2006, there were no single issuer investments that exceeded 5% of the STIP portfolio. At June 30, 2006, MGSLP owned 8,878,038 units valued at \$1 per unit for a total of \$8,878,038. During fiscal year 2006, MGSLP had STIP investment earnings of \$437,099. STIP securities include Banker's Acceptances, Commercial Paper, Corporate Obligations, Montana Certificates of Deposit, Government Securities, and Repurchase Agreements. At June 30, 2006, most securities, were held by the state or its agent in the state's name. The remaining portions not classified were loaned under a security lending agreement with the state's agent.

Asset-backed securities have less credit risk than securities not backed by pledged assets and market risk for these securities is the same as market risk for similar non asset-backed securities. While variable-rate securities have credit risk identical to similar fixed-rate securities, their market risk is more sensitive to interest rate changes. Market risk may be less volatile than fixed-rate securities because the value of variable-rate securities will usually remain at or near par. There are no legal risks that the Board of Investments is aware of regarding any STIP investments.

According to the Governmental Accounting Standards Board (GASB) Statement No. 31, Accounting and Financial Reporting for Certain Investments and External Investment Pools, STIP is considered an external investment pool. An external investment pool is defined as an arrangement that pools the monies of more than one legally separate entity and invests, on the participant's behalf, in an investment portfolio. STIP is also classified as a "2a7-like" pool. A 2a7-like pool is an external investment pool that is not registered with the Securities and Exchange Commission (SEC) as an investment company, but has a policy that it will, and does, operate in a manner consistent with the SEC's Rule 2a7 of the Investment Company Act of 1940. If certain conditions are met, 2a7-like pools are allowed to use amortized cost rather than fair value to report net assets to compute unit values. The Board of Investments has adopted a policy to treat STIP as a 2a7-like pool.

3. DUE FROM FEDERAL GOVERNMENT

MGSLP pays individual lending institutions for any loans that have defaulted or are unpaid due to the death, permanent disability, or bankruptcy of the borrower. The agency then seeks reimbursement from the DE in accordance with reinsurance agreements between the agency and DE. Claim payments and subsequent reinsurance payments are paid from and deposited into the Federal Student Loan Reserve Fund. MGSLP's claims for reinsurance payments not received as of June 30, 2006, are included here.

In addition, the receivable Due From Federal Government includes amounts MGSLP had not yet received for Loan Processing and Issuance Fees (Note 9) for the last quarter of fiscal year 2006. The extent of the outstanding reinsurance activity and other pending reimbursements from DE as of June 30, 2006, is shown below.

Reinsurance Claims	\$3,168,552	Federal Student Loan Reserve Fund
Teacher Loan Forgiveness	\$17,964	Agency Operating Fund
Loan Processing and Issuance Fee	32,372	Agency Operating Fund
Total Due From Federal Government	<u>\$3,218,888</u>	

4. LONG TERM INVESTMENTS

MGSLP maintains an account with the Montana Family Education Savings Program (MFESP) for funds held in trust for recipients of MGSLP's essay scholarship contest. All

funds at MFESP are invested in certificates of deposit of varying maturity dates. As of June 30, 2006, the balance of the certificates of deposit totaled \$26,341 (\$22,500 in face value plus \$3,841 in paid or accrued interest through June 30, 2006).

5. PROPERTY HELD IN TRUST

MGSLP operates an escrow disbursement service for approximately fifty lenders. Participating lenders are assessed a fee for this service. In accordance with contracts MGSLP has with the disbursement service lenders, MGSLP automatically debits the lenders' accounts to collect loan proceeds. MGSLP then disburses funds to the schools for delivery to the students either by individual State of Montana warrants or electronic transfers. The MGSLP disbursement service records all adjustments to individual student loan accounts and ensures that school refunds of loan proceeds are promptly returned to the lenders. As of June 30, 2006, MGSLP's disbursement service held \$183,577 in student loan funds that are to be refunded to lenders after June 30, 2006. Disbursement service revenues earned during fiscal year 2006 were \$167,796.

6. DUE TO FEDERAL GOVERNMENT

After assignment to the guaranty agency, MGSLP seeks collection of student loans that have defaulted. A portion of the recoveries of loans reinsured by the Department of Education (DE) is owed back to DE (Note 12). At June 30, 2006, the amount owed to DE was \$708,883.

7. DESIGNATED FUND BALANCE

During fiscal year 2003, the Department of Education (DE) allowed guaranty agencies to transfer any unspent recall interest earned during prior fiscal years from the Federal Student Loan Reserve Fund to the Agency Operating Fund. The total amount of funds transferred at that time was \$820,346. The agency is authorized to use these earnings from the Agency Operating Fund to perform certain default reduction activities, as outlined in the Balanced Budget Act of 1997. As of June 30, 2006, the unspent portion of these designated earnings was \$816,047.

8. GUARANTEE FEE INCOME

Guarantee fees are received from borrowers at the time loans are disbursed. As of July 1, 1994, the maximum guarantee fee that borrowers may be charged is 1% of the loan amount.

During fiscal year 2006, MGSLP charged a guarantee fee of 1%. The fees are deposited into the Federal Student Loan Reserve Fund (FSLRF), and recognized as revenue upon receipt. Guarantee fee revenue for fiscal year 2006 was \$1,624,506.

9. LOAN PROCESSING AND ISSUANCE FEE

The Higher Education Amendments of 1998 authorized payment of a Loan Processing and Issuance Fee beginning October 1, 1998. Under this Act, each guaranty agency is paid a loan processing and issuance fee, to be deposited into the Agency Operating Fund, equal to .65% of the total principal amount of loans originated during federal fiscal years 1999-2003 on which the agency issued insurance. Beginning in federal fiscal year 2004, for loans guaranteed on or after October 1, 2003, the fee dropped to .40%. During fiscal year 2006, Loan Processing and Issuance Fee revenue totaled \$657,639 which includes \$32,372 accrued for reimbursements that were not received until after June 30, 2006.

10. ACCOUNT MAINTENANCE FEE

The Higher Education Amendments of 1998 authorized the payment of an Account Maintenance Fee beginning October 1, 1998. Under this Act, each guaranty agency is paid an account maintenance fee, to be deposited into the Agency Operating Fund. For federal fiscal years beginning 2001, the fee is .10% of the original principal balance of guaranteed loans outstanding during the year. During fiscal year 2006, Account Maintenance Fee revenue totaled \$1,829,196 of which \$1,343,136 was authorized for payment from the Federal Student Loan Reserve Fund by the Department of Education.

11. DEFAULT AVERSION FEE

The Higher Education Amendments of 1998 authorized the payment of a Default Aversion Fee beginning October 1, 1998. Upon receipt of a completed lender request for assistance (LRA) not earlier than the 60th day of delinquency, a guaranty agency must engage in default aversion activities designed to prevent a default by the borrower. Department of Education Regulations provide for payment of a fee equal to 1% of the loan balance at the time an LRA is submitted, regardless of whether or not the loan is brought current. The default aversion fees are to be transferred from the Federal Student Loan Reserve Fund (FSLRF) to the Agency Operating Fund (AOF) no more frequently than monthly. If the agency receives a default aversion fee and the account later defaults, the agency must rebate 1% of the claim amount to the FSLRF. The fee may be paid only once on any loan. During fiscal year 2006, net Default Aversion Fee revenue and expense, for the AOF and FSLRF respectively, was \$1,006,662.

12. COLLECTION COSTS RETAINED

MGSLP pursues collection, from the borrower or other responsible party, of defaulted loans held by the agency. The U.S. Secretary of Education is entitled to his equitable share of any recoveries, as determined by the rate of reinsurance on the defaulted loans less an allowance for collection cost reimbursement. Beginning October 1, 2003, the Higher Education Amendments of 1998 authorize guaranty agencies to deposit an amount equal to 23% of the payments made by or on behalf of a defaulted borrower into its Agency Operating Fund. In addition, the Secretary provides the agency with collection costs amounting to 18.5% of the outstanding balance of any defaulted loan held by the agency which is consolidated by the borrower into a Federal Consolidation Loan through either Federal Family Education Loan Program (FFELP) consolidation or Federal Direct Student Loan Program (FDSLSP) consolidation. During fiscal year 2006, MGSLP retained \$2,716,791 in net collection costs from loan recoveries and consolidations, as follows.

	Revenues	Expenses	Net
Collection Recoveries	\$3,392,027	\$2,613,984	\$778,043
Rehabilitations	\$2,699,117	\$1,848,648	\$850,469
FFELP Consolidations	\$0	\$0	\$0
FDSLSP Consolidations	<u>\$1,088,279</u>	<u>\$0</u>	<u>\$1,088,279</u>
Total	<u>\$7,179,423</u>	<u>\$4,462,632</u>	<u>\$2,716,791</u>

13. CLAIMS PAID TO LENDERS AND REINSURANCE FROM DEPARTMENT OF EDUCATION

MGSLP records amounts paid to lenders for claims and subsequent amounts received from the Department of Education (DE) as expenses and revenues respectively. For fiscal year 2006, MGSLP paid claims totaling \$17,504,608 and received reinsurance from DE totaling \$17,003,774.

14. TRANSFER OF ESSAY CONTEST SCHOLARSHIP FUNDS

During fiscal year 2006, the agency transferred those dollars committed for scholarships for the winners of the MGSLP Essay Contest from the Agency Operating Fund to the Essay Scholarship Fund. The total amount transferred during fiscal year 2006 was \$36,600.

15. SUBSEQUENT EVENTS & CONTINGENCIES – RECALL OF FEDERAL RESERVES

The Higher Education Amendments of 1998 required the Secretary to recall from guaranty agency federal student loan reserve funds a total of \$85 million, \$82.5 million, and \$82.5 million in each of federal fiscal years 2002, 2006, and 2007 respectively. On August 28, 2002, DE made a final determination of MGSLP's share of the total amounts to be recalled for each of the stated federal fiscal years: FFY2002 at \$394,414, FFY2006 at \$382,814, FFY2007 at \$382,813. The amount due for FFY2006 was transferred to the Secretary in August 2006. The remaining amount for FFY2007 is scheduled to be transferred to the Secretary no later than September 1, 2007.

16. CONTINGENCIES

The original principal balance of guaranteed loans outstanding held by MGSLP as of June 30, 2006, was approximately \$1,639,865,033. This amount excludes bad debt, death, disability, and bankruptcy claims which have been previously purchased by the agency. MGSLP has entered into agreements with the Department of Education (DE), dated June 13, 1980, for reinsurance and supplemental reinsurance of loans, in accordance with the Higher Education Act of 1965, as amended. These agreements allow for 100% reimbursement by DE for claims due to the death, disability, or bankruptcy of the borrower. Claims paid due to defaulted loans may be reimbursed by DE for up to 100%. The percent of reimbursement on defaulted loans payable to the agency is dependent upon MGSLP's annual default rate and date of the loan's first disbursement. Annual default rates are calculated as the ratio of year-to-date default purchases divided by the original guaranteed amount of loans in repayment status at the beginning of the federal fiscal year.

The following schedule reflects the federal reinsurance rates on defaulted student loans. In the event of extreme future adverse loss experience, MGSLP could be liable for up to 25% of the outstanding loan volume. Since its inception, MGSLP has paid \$3,653,043 in claims, or portions of claim eligible loans, which were not reinsured by DE. During fiscal year 2006, MGSLP recovered \$169,804 of the total outstanding balance of non-reinsured claims held by the agency.

RATE OF ANNUAL DEFAULTS	FEDERAL REINSURANCE On loans made prior to 10/01/93	FEDERAL REINSURANCE On loans made on or after 10/01/93 and prior to 10/01/98	FEDERAL REINSURANCE On loans made after 10/01/98
Less than 5%	100%	98%	95%
5% or greater but less than 9%	90% of claims 5% or greater but less than 9%	88% of claims 5% or greater but less than 9%	85% of claims 5% or greater but less than 9%
9% or greater	80% of claims 9% or greater	78% of claims 9% or greater	75% of claims 9% or greater

17. COMMITMENTS

MGSLP is bound by Guarantee Reserve Agreements with the lending institutions participating in the Federal Family Education Loan Program in Montana. These agreements require MGSLP to maintain an amount in the guarantee reserve fund equal to at least 0.25% of the unpaid principal balance of all outstanding loans guaranteed by the agency.

The Guarantee Reserve Agreement ensures that MGSLP will have sufficient cash available to carry out its reasonably expected obligations on guaranteed claim eligible student loans. As of June 30, 2006, MGSLP was in compliance with all Guarantee Reserve Agreements.

18. RELATED PARTY TRANSACTIONS

The Montana Board of Regents, which governs MGSLP, guarantees loans owned by the Montana Higher Education Student Assistance Corporation (MHESAC). The Board of Regents and MHESAC have four common board members. Approximately 75.74% of MGSLP's outstanding loan volume is held by MHESAC.

MGSLP also has an agreement with Student Assistance Foundation of Montana (SAF) to share certain costs for the lease of computer equipment; computer and software maintenance costs; and personnel costs for employees of SAF who perform services that are of direct benefit to MGSLP. Certain SAF personnel are authorized to purchase computer equipment for use by both MGSLP and SAF. Costs for these purchases are covered under an agreement for services between the two entities. During fiscal year 2006, MGSLP's portion of shared costs reimbursed to SAF was \$401,664. The Board of Regents and SAF have four common board members.

19. EMPLOYEES' RETIREMENT SYSTEM

MGSLP classified employees are provided a retirement program through the Montana Public Employees' Retirement System (PERS). Professional employees with contracts under the authority of the Board of Regents are covered by the Optional Retirement Program (ORP), which is available through the Teachers Insurance and Annuity Association-College Retirement Equities Fund (TIAA-CREF).

Defined Benefit Plans

Established in 1945 and governed by Title 19, chapter 3, MCA, PERS participants are eligible to retire at age 60 with at least five years of service; at age 65 regardless of length of service; or at 30 years of service regardless of age. A reduced retirement benefit may be taken with 25 years of service or at age 50 with a minimum of five years of service. Effective January 1, 1989, monthly retirement benefits are calculated by taking 1/56 times the years of service times the final average salary. Vesting occurs once membership service totals five years.

Defined Contribution Plan

ORP was established in 1988 and is underwritten by the Teacher's Insurance and Annuity Association – College Retirement Equities Fund (TIAA-CREF). The ORP is a defined-contribution plan. Until July 1, 2002, only faculty and staff with contracts under the authority of the Board of Regents were eligible to participate. The plan was changed, effective July 1, 2003, to allow all staff to participate in the ORP. Contribution rates for the plan are required and determined by State law. MGSLP's contributions were equal to the required contribution. The benefits at retirement depend upon the amount of contributions, amounts of investment gains and losses, and the employee's life expectancy at retirement. Under the ORP, each employee enters into an individual contract with TIAA-CREF. MGSLP records employee/employer contributions and remits monies to TIAA-CREF. Individuals vest immediately in the employer portion of retirement contributions. Annual reports that include financial statements and required supplemental information on the plan are available directly from TIAA-CREF.

According to state law, MGSLP also remits additional employer contributions to the PERS and TRS to amortize past service unfunded liability.

Professional Staff	
Covered Payroll	150,926
Employer Contributions	7,480
Percent of Covered Payroll	4.96%
Employee Contributions	10,631
Percent of Covered Payroll	7.04%
Additional Employer to TRS	6,097
Total Employer Contribution	9.00%
Staff:	
Covered Payroll	1,452,430
Employer Contributions	100,218
Percent of Covered Payroll	6.90%
Employee Contributions	100,218
Percent of Covered Payroll	6.90%



Montana Guaranteed Student Loan Program

2500 Broadway P.O. Box 203101
Helena, MT 59620-3101
Phone: (406) 444-6594 Fax: (406) 444-1869
Customer Assistance: (800) 537-7508
www.mgslp.state.mt.us

October 24, 2006

Scott Seacat, Legislative Auditor
Room 160, State Capitol
PO Box 201705
Helena, MT 59620-1705

RECEIVED

OCT 25 2006

LEGISLATIVE AUDIT DIV.

Dear Mr. Seacat:

We have received the results of the fiscal audit for the year ending June 30, 2006, and consider the audit completed. The report contains the audited financial statements and accompanying notes for the fiscal year. The financial statements received an unqualified opinion and there are no findings or recommendations.

We would like to take this opportunity to thank your office and, in particular, Alexa O'Dell – the senior auditor primarily responsible for the audit. Alexa is thorough, professional, and always mindful of the work we must complete in order to serve our Montana residents.

The mission of the Montana Guaranteed Student Loan Program is to improve access to higher education. We guarantee student loans, administer a variety of state and federal grant and scholarship programs, and also manage the Montana Family Education Savings Program. Our citizens can take comfort knowing they can rely on the financial information reported in our financial statements and accompanying notes.

Once again, thank you for your assistance.

Sincerely,

Bruce Marks
Director, Montana Guaranteed Student Loan Program

